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REPORT ON EXAMINATION
OF THE
NATIONAL TRUST INSURANCE COMPANY
SARASOTA, FLORIDA

AS OF
DECEMBER 31, 2002

THE DEPARTMENT OF COMMERCE AND INSURANCE
STATE OF TENNESSEE
NASHVILLE, TENNESSEE

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Sarasota, Florida
August 17, 2004

Honorable Kevin McCarty
Chair, Financial Condition (E) Committee
Secretary, Southeastern Zone
National Association of Insurance Commissioners
Director, Office of Insurance Regulation
Florida Department of Financial Services
200 East Gaines Street
Tallahassee, FL 34399

Honorable Paula Flowers
Commissioner
State of Tennessee
Department of Commerce and Insurance
Nashville, Tennessee 37243

Dear Commissioners:

Pursuant to your instructions and in accordance with Tennessee insurance laws, regulations, and resolutions adopted by the National Association Insurance Commissioners (NAIC), a financial examination and market conduct review have been made of the condition and affairs of the

NATIONAL TRUST INSURANCE COMPANY
A TENNESSEE CORPORATION
with Administrative Offices in
SARASOTA, FLORIDA

hereinafter and generally referred to as the Company, and a report thereon is submitted as follows:

INTRODUCTION

This examination was called by the Commissioner of Commerce and Insurance of the State of Tennessee through the Examination Tracking System of the National Association Commissioners (NAIC) and commenced on September 4, 2003. The examination was conducted under the association plan of the NAIC by duly authorized representatives of the Tennessee Department of Commerce and Insurance.

SCOPE OF EXAMINATION

This examination report covers the period from December 31, 1999, the date of the last previous examination, to the close of business on December 31, 2002, and includes any material transactions and/or events occurring subsequent to the examination date and noted during the course of the examination.

The examination of the financial condition was conducted in accordance with guidelines and procedures contained in the National Association of Insurance Commissioners (NAIC) Examiners Handbook. During the course of examination, assets were verified and valued and liabilities were determined and estimated as of December 31, 2002. The financial condition of the Company and its amount of solvency were thereby established. Test checks were made of income and disbursement items for selected periods, and a general review was made of the Company's operations, practices, and compliance with applicable statutes and regulations. All asset and liability items contained in the financial statement of this report were examined and verified with relative emphasis according to their amount and potential impact on capital and surplus.

In addition, the following topics were reviewed:

- Previous Examination Comments and Recommendations
- Company History
- Charter and Bylaws
- Management and Control
- Pecuniary Interest
- Corporate Records
- Fidelity Bonds and Other Insurance
- Territory
- Plan of Operation
- Market Conduct Activities
- Reinsurance
- Commission Equity
- Retirement Plan and Other Employee Benefits
- Loss Experience
- Accounts and Records
- Statutory Deposits
- Agreements with Parent, Subsidiaries and Affiliates
- Litigation
- Financial Statement

They are discussed in detail as follows:

PREVIOUS EXAMINATION COMMENTS AND RECOMMENDATIONS

The previous full scope examination of the Company was conducted as of December 31, 1997, by examiners of the Department of Commerce and Insurance, State of Tennessee. It reported six changes to the Company's financial statement and six adverse findings. The adverse findings and their resolutions are as follows:

- *The view of premium aging in the Other Than Comp (OTC) business has been complicated to extract.*

As noted in the previous examination report, the Company has installed the Allenbrook System using Phoenix software to eventually eliminate this problem. The old business continues to runoff through the Freedom system.

- *The Company is now nonadmitting the receivable from parent on quarterly statements filed with the Department. These amounts are related to premium remittances which are received via a lockbox and deposited into a fiduciary account under the name of FCCI Insurance Company.*

The Company and FCCI have entered into a written agreement specifying that amounts due are to be settled monthly, thereby reducing the need to nonadmit receivables from parent.

- *The Company is a party to an intercompany service agreement for the provision of claims servicing, managing payroll and providing clerical and administrative assistance with FCCI Claims Services, Inc. (FSI), an affiliated corporation. To more accurately reflect NAIC Accounting Practices, the Company should record any amount owed to FSI on the liability line captioned "Payable to parent, subsidiaries and affiliates". The referenced accounting practice states "unreimbursed expenditures on behalf of the company by a parent, affiliate or subsidiary or amounts owing through other intercompany transactions" are to be included on the liability line captioned, "Payable to parent, subsidiaries and affiliates".*

The Company continues to report these amounts as "Other expenses".

- *The intercompany service agreement calls for settlement on a monthly basis. Settlement has been occurring quarterly. The Company should either settle monthly or amend the agreement to indicate settlement on a quarterly basis.*

The Company has not amended the agreement. Amounts are sometimes settled monthly, but the agreement is not strictly adhered to.

- *In July of 1999, the Company entered into a lockbox arrangement with its parent, FCCI Insurance Company whereby premium remittances are deposited into a fiduciary account under the name of FCCI Insurance Company. The funds are electronically identified, using encoded remittance advises. Transfer of funds to the Company from FCCI have been taking place on a quarterly basis. There is no formal written agreement which outlines settlement terms.*

The Company and FCCI should formalize the lockbox arrangement with a written intercompany agreement. Transfer should take place on a monthly rather than quarterly basis which will reduce or eliminate the need to nonadmit the "Receivable from parent".

The Company and FCCI have formalized the lockbox arrangement with a written agreement. Amounts are sometimes settled on a monthly basis, but the agreement is not strictly adhered to.

- *The Custody Agreement with the Bank of New York covering bonds and short-term investments did not contain the required language as referenced in Regulation 0780-1-46.04 as follows "That such custodial agreement provide a standard of responsibility on the part of the custodian which shall not be less than the responsibility of a bailee for hire or a fiduciary under statutory or case law of Tennessee, that securities held by the custodian are subject to instructions of the insurance company; and that securities may be withdrawn immediately upon demand of the insurance company".*

The Company was also made aware of the department's exception to the offset clause in the Custody Agreement with Bank of New York that could be invoked if the Company had not honored all of its obligations to the Custodian. The Company was also informed that there was a reference to the Florida Department of Insurance in the wording of the agreement which should not be included in the agreement.

It was recommended to the Company during the course of the examination that the agreement be modified to comply with Regulation 0780-1-46.04. The Company's legal staff and Bank of New York worked with the department to formulate a proposed amendment and supplement to the custody agreement to effect the suggested changes.

The Company has entered into a custody agreement with the Bank of New York which meets the requirements of Tennessee Regulation 0780-1-46.04.

- *The Quota Share Reinsurance Agreement between the Company and its parent, FCCI Insurance Company was modified by virtue of an endorsement effective January 1, 1998 during 1999 and was not submitted for department approval as required under TCA 56-11-206(a)(2)(C). The Company submitted the agreement*

for approval during the course of this examination. The original agreement had been approved by the department in January, 1997.

It does not appear that the amendment was properly submitted for approval as requested by the examiners. The Company could not provide evidence of either its submission or approval.

COMPANY HISTORY

The Company, then known as National Trust Fire Insurance Company, was incorporated January 14, 1965, under the laws of the State of Tennessee and commenced business January 25, 1965, with capital paid up of \$400,000 and paid in surplus of \$350,000. The Company's authorized capital stock is \$1,000,000 divided into 10,000 shares of \$100 par value.

The Company's charter authorizes it to operate generally as a fire and marine insurance company with powers also to write casualty insurance including workers' compensation and to assume reinsurance.

On April 20, 1972, the stockholders, at a special meeting, approved a stock dividend of 1,000 shares. On November 7, 1979, at a special meeting, the board of directors approved a stock dividend of 3,500 shares from paid in and contributed surplus to capital paid up. Thus, there existed \$850,000 in capital paid up and \$0 in paid in and contributed surplus.

On April 23, 1980, National Trust Life Insurance Company (former parent of the Company) and Commonwealth Life Insurance Company, Louisville, Kentucky merged and Commonwealth became the surviving company. On the date of the merger, Commonwealth acquired all of the issued and outstanding stock of the Company; however, no new stock certificate was issued to Commonwealth. Certificates #1 dated January 13, 1965, #2 dated April 20, 1972 and #3 dated November 7, 1979, aggregating 8,500 shares, issued to National Trust Life Insurance Company, were held by Commonwealth as evidence of ownership.

Effective May 7, 1987, National Trust Fire Insurance Holdings, Inc. a Georgia Corporation acquired all the authorized capital stock of the Company comprised of one million dollars (\$1,000,000) divided into ten thousand (10,000) shares with a par value of \$100 each. Eighty-five hundred (8,500) shares were owned by National Trust Life Insurance Company at the acquisition date.

Subsequent to the acquisition date of May 7, 1987, the Company ceased to write any new business and did not issue any new policies through 1990, but maintained the Certificates of Authority to write business in four southeastern states.

In 1990, the Company was sold to Florida Employers Life Insurance Corporation (FELIC), which assumed all of the existing liabilities of the Company. The Company's name was changed to National Trust Insurance Company effective July 6, 1990. FELIC was formed in 1988 as a stock life insurer and is a wholly owned subsidiary of FEICO Agency, Inc. (FEICO Agency). On January 12, 1990, FEICO acquired all of the outstanding stock of the Company for a purchase price of \$2,240,293. FEICO Agency borrowed \$3,000,000 from Florida Construction, Commerce and Industry Self Insurers Fund (FCCI) to complete the acquisition and provide additional capital for the Company through FELIC. The \$3,000,000 obligation of FEICO Agency was paid in full during 1991.

On March 31, 1992, the Florida Employers Insurance Company (FEICO) sold all of its assets, including its indirect ownership of all of the Company's common stock to FCCI Investment Group, Inc., a wholly owned subsidiary of FCCI pursuant to the terms of a definitive acquisition agreement executed in August, 1991. FCCI Investment Group, Inc. assumed all of the liabilities and obligations of FEICO including those of the Company and continued the underwriting operations and businesses of the Company.

Regulatory approval of the transaction by the Florida Department of Labor and Department of Insurance was contingent upon FCCI's disposal of two subsidiaries, National Trust Insurance Company and FELIC, within eighteen months of acquisition. A twelve month extension was granted to October 1, 1994 to complete the divestiture or liquidation of these businesses. Both companies ceased writing new insurance policies effective October 1, 1993.

During 1991, the Company began writing direct commercial property and casualty insurance, primarily workers' compensation, in Georgia as part of the organization's long range plan to expand its products and services into other southeastern states.

Participation in the State of Georgia direct workers' compensation market required participation in the State of Georgia Assigned Risk Plan. This plan requires that workers' compensation insurers share proportionally in relation to their total premiums in the state in providing insurance coverage for certain high-risk insureds.

In July of 1992, due to statutory changes in the State of Georgia, the Company increased their authorized number of shares of common stock to fifty thousand (50,000) shares with a par value of \$100.00 per share and issued five thousand (5,000) shares to FELIC to increase the Company's paid-in capital to \$1,500,000. After the transaction, FELIC owned all of the Company's issued and outstanding common stock totaling fifteen thousand (15,000) shares. These changes were amended to the Company's charter on July 24, 1992.

On November 16, 1994, the Florida Department of Insurance approved a consent order permitting FCCI Self Insurance Fund to reorganize from a self insurance fund to a mutual company. FCCI Self Insurance Fund was renamed FCCI Mutual Insurance

Company. This consent order vacated the previous requirement for FCCI to divest of the two insurance subsidiaries, including National Trust Insurance Company.

In December, 1995, the Company was sold by its parent (Florida Employers Life Insurance Corporation) to an upstream holding company, FCCI Investment Group, Inc. (FIG) for \$3,790,293, an amount equal to FELIC's original cost of the common stock. FIG then made an additional capital contribution of \$8,000,000 in December, 1995. During 1996, FCCI Investment Group, Inc. changed its name to FCCI Insurance Group, Inc.

In May of 1997, the Company capitalized \$300,000 of contributed surplus in the form of a stock dividend of 3,000 shares of common stock to FCCI Insurance Group, Inc. (its parent). In April of 1998, the Company capitalized \$700,000 of contributed surplus in the form of a stock dividend of 7,000 shares of common stock to its parent.

As of December 31, 2002, the Company reported common capital stock of \$2,500,000, gross paid-in and contributed surplus of \$9,290,293, and unassigned funds of (\$3,264,993).

The Company utilizes the underwriting and administration expertise that has been developed by its affiliate, FCCI Services, Inc. (FSI), to select and manage preferred commercial risks. The company has no employees. All product support and general and administrative services are provided by FSI. FSI provides claims and other insurance administrative services to several clients, with its primary client being FCCI.

At December 31, 2002, the Company was licensed in 19 states.

Growth and Financial History:

The following exhibit depicts certain aspects of the growth and financial history of the Company since the previous examination, according to annual statements filed with the Tennessee Department of Commerce and Insurance.

Year	Earned Premiums	Incurred Losses	Admitted Assets	Liabilities	Capital and Surplus
2000	\$2,426,152	\$1,623,711	\$57,662,780	\$46,032,234	\$11,630,546
2001	6,452,431	4,473,660	90,134,224	78,844,547	11,289,677
2002	5,501,138	5,765,032	35,484,375	26,959,075	8,525,300

CHARTER AND BYLAWS

Charter:

The original Charter was filed and recorded with the Tennessee Secretary of State on January 14, 1965, and recorded with the Shelby County Clerk on January 15, 1965. It was previously amended on November 16, 1989, August 7, 1990 and July 24, 1992.

The amended Charter authorizes the corporation "to transact business pertaining to the providing of insurance and any business activities reasonably incidental to such insurance business as authorized under the provisions of the Tennessee Statutes." It authorizes the Company to issue fifty thousand share of common stock at a par value of \$100.00 per share and requires that paid-in capital be no less than \$1,500,000. The corporation's existence is perpetual.

The amended Charter also provides that the principal office of the Company may be changed by the Board of Directors to any other location in Florida. The Company was relocated to 6300 University Parkway, Sarasota, Florida in May, 2001. There were no charter amendments during the period under examination.

By-Laws:

The by-laws of the Company that were in effect at December 31, 2002 were amended by the unanimous consent of the Board on January 25, 1996 in order to increase the number of directors to not more than eleven (11) persons nor less than five (5) persons.

All vacancies in the Board of Directors shall be filled by the remaining Directors, by a majority vote. A quorum at all meetings of the Board of Directors shall consist of a majority of the whole Board. The Directors have the authority to fix the compensation of each of the Directors. The By-Laws can be amended by a majority vote of the Board at a regular or special meeting or at any time by a unanimous consent expressed in writing.

An annual meeting of shareholders shall be held in July of each year at any place within or without the State of Tennessee. Special meetings of the shareholders may be called by the Board of Directors or holders of at least ten percent (10%) of the entire capital stock of the Corporation issued and outstanding and entitled to vote.

Regular meetings of the Board of Directors may be held at any place or places within or without the State of Florida, on such days and at such hours as the Board may by resolution, appoint. Special meetings may be called by the Chairman, the President or by any two members of the Board and may be held at any place and at any time.

The Officers of the Company shall be chosen by the Board of Directors and include a President, Secretary, Treasurer and such other officers as may be appointed. The

general duties of officers are further defined by Article III of the By-Laws. The salary of the President shall be fixed by the Board of Directors. Salaries of all other officers shall be fixed by the President unless otherwise fixed by the Board of Directors.

The By-Laws also contain certain corporate responsibilities relating to dividends and finances, books and records and indemnification of officers and directors.

MANAGEMENT AND CONTROL

Management:

The By-Laws vest the management of the business and affairs of the Company in a Board of Directors of at least five (5) and not more than eleven (11) persons. As of December 31, 2002, the Board of Directors of the Company was composed of the following:

Albert Lee Conyers
Russell Ashmore Currin, Jr.
Robert Winthrop Flanders
Harvey Ronald Foxworthy
William Eugene Getzen
Marvin Steven Haber
Gordon William Jacobs
John Thomas Stafford
Charles Edward Stottlemeyer

As of December 31, 2002, the following persons held office in the Company:

Gordon William Jacobs, President
Robert Emmett McManus, Secretary
Charles Joseph Bachand, Treasurer

The administrative and executive functions of the Company are performed by its home office staff employed through FCCI Services, Inc. (FSI). FSI was known as Florida Employers Insurance Service Corporation until January 1, 2001 when it adopted its present name. Certain services are purchased from outside contractors if needed and are not available from in house personnel. Such services include actuarial analysis and independent audit.

Control:

The Company is wholly-owned by FCCI Insurance Group Inc., a Florida insurance holding company. FCCI Insurance Group Inc. is a 100% owned subsidiary of FCCI Insurance Company, which is a Florida domestic insurer, with the ultimate parent being FCCI Mutual Insurance Holding Company.

During the period under examination, the Company did not pay any dividends to its stockholder.

A holding company organizational chart is included at the last page of this examination report.

PECUNIARY INTEREST TENN. CODE ANN. §56-3-103

During the period under examination, the Company had an established procedure for disclosure to its Board of Directors of any material interest or affiliation on the part of its officers and directors which conflicts with the person's official duties with the Company. Statements regarding such conflicts of interest were executed by the officers and directors on an annual basis. The statements were reviewed and the noted disclosures were deemed immaterial.

CORPORATE RECORDS

Minutes of meetings of the shareholders and Board of Directors of the Company were reviewed for the period under examination. In general, such minutes appear to be in proper order and accurately report the proceedings of each respective meeting.

FIDELITY BOND AND OTHER INSURANCE

The Company was included as a named insured on the following coverages which were in effect at December 31, 2002:

<u>TYPE OF COVERAGE</u>	<u>STATED AMOUNT</u>
Fidelity Insurance	Employee Dishonesty \$500,000, Forgery or Alteration \$100,000, Deductible \$5,000
General Liability	\$1,000,000 Each Occurrence, \$2,000,000 General Aggregate (includes Products & Completed Operations) \$1,000,000 Personal Injury, \$10,000 Medical Expense
Professional Liability	\$10,000,000 Each Occurrence and Aggregate \$500,000 Retention per Occurrence
Umbrella Liability	\$10,000,000 Each Occurrence and Aggregate Coverage B Retention \$10,000

The Company's fidelity bond was in excess of the suggested minimum amount as

recommended by the National Association of Insurance Commissioners Financial Examiners Handbook. The insurers providing the above-listed coverages were licensed to operate in both Tennessee and Florida.

TERRITORY

As of December 31, 2002, and as of the date of this examination report, the Company was licensed to transact business in the States of Tennessee, Alabama, Arizona, Arkansas, Florida, Georgia, Indiana, Iowa, Kansas, Kentucky, Louisiana, Mississippi, Missouri, Nebraska, North Carolina, Ohio, Oklahoma, South Carolina, and Virginia. Certificates of Authority for the jurisdictions were reviewed and found to be in order.

PLAN OF OPERATION

The Company intends to be a regional commercial carrier in the Southeast marketing its products through a combination of independent agents and managing general agents which contract with multiple independent agents. The Company presently writes workers' compensation coverages as well as various commercial property and casualty coverages.

During 2002, the Company wrote direct premium as follows:

<u>State</u>	<u>Direct Premiums Written</u>	<u>Direct Premiums Earned</u>	<u>Direct Losses Paid</u>	<u>Direct Losses Incurred</u>	<u>Direct Losses Unpaid</u>	<u>Finance & Service Charges</u>
Alabama	\$ 4,724,000	\$ 4,850,119	\$ 2,121,540	\$ 3,917,567	\$ 8,251,551	\$ 0
Arizona	0	0	0	0	0	0
Arkansas	2,329,748	4,124,332	9,220,646	9,080,655	10,507,372	0
Florida	13,206,554	17,281,231	7,405,968	13,427,050	27,529,051	102,807
Georgia	18,765,197	16,370,992	7,007,266	8,839,920	12,595,513	0
Indiana	0	0	0	0	0	0
Iowa	0	0	0	0	0	0
Kansas	0	0	0	0	0	0
Kentucky	1,742,670	2,623,550	2,953,058	5,530,903	5,311,226	0
Louisiana	636,702	508,730	45,378	106,431	122,359	0
Mississippi	425,679	446,910	970,872	115,453	1,760,532	0
Missouri	0	0	0	0	0	0
Nebraska	0	0	0	0	0	0
North Carolina	1,035,073	310,859	28,134	75,891	47,757	0
Ohio	0	0	0	0	0	0

Oklahoma	0	0	0	0	0	0
South Carolina	511,913	323,863	94,292	474,095	379,804	0
Tennessee	(2,528,349)	1,919,051	3,084,499	3,952,530	8,822,259	0
Virginia	<u>208</u>	<u>215</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Total	<u>\$40,849,415</u>	<u>\$48,759,852</u>	<u>\$ 32,931,653</u>	<u>\$45,520,495</u>	<u>\$75,327,424</u>	<u>\$ 102,807</u>

The total direct premium written through Managing General Agents in 2002 was \$2,481,273. MGAs writing greater than 5% of surplus were The Insurance Link of America, LLC (LINK), who wrote \$1,844,571 in direct premium and National Loss Control Management (NLCM) who wrote \$636,702 in direct premium. LINK wrote its premiums in Tennessee, Kentucky, Arkansas and Alabama. LINK is not licensed as an MGA in Tennessee, Kentucky or Arkansas, but was licensed as an MGA in Alabama. Its president, Charles E. Link, is licensed as an agent in all states in which LINK wrote premium, which appears to meet the requirements of Tenn. Code Ann. §56-6-503 (a) and (b). NLCM is licensed as an MGA in Louisiana, the only state in which it writes business.

It was noted that the Company entered into a Termination Agreement with LINK on August 15, 2002.

MARKET CONDUCT ACTIVITIES

In accordance with the policy of the Tennessee Department of Commerce and Insurance, a market conduct review was made of the Company as of December 31, 2002 in conjunction with this examination. The following items were addressed:

Policy Forms, Rating and Underwriting:

Under Tennessee Code Annotated, Section 56-5-306, rates, supplementary rate information, policy forms and endorsements will be filed with the Commissioner not later than fifteen (15) days after the effective date. A sample of forms and rates currently in use was reviewed and appeared to be properly filed with the respective states. It appears that the Company adheres to its underwriting standards.

Advertising:

The advertising material currently in use was reviewed and found to be in order.

Claims Review:

A sample of open and closed claim files reviewed during the examination indicated that claims were being paid in accordance with policy provisions and settlements were made promptly upon receipt of proper evidence of the Company's liability.

Policyholder Complaints:

A review of complaints made to regulatory authorities regarding the Company indicated an effort by the Company to equitably fulfill its obligations and to resolve policyholder complaints in a timely manner.

Privacy Policy:

The Company has a written privacy policy. It is supplied to its policyholders the first time business is transacted and annually thereafter in compliance with Tenn. Comp. R. & Regs. Tit. Dep't of Commerce and Ins., ch. 0890-1-72.

REINSURANCE

The Company's reinsurance agreements were reviewed and found to contain the standard provisions for arbitration, cancellation, errors and omissions, exclusions, insolvency offset, settlement, taxes and termination. The following is a summary of the reinsurance agreements in effect as of December 31, 2002:

Assumed:

(1)

<u>Type:</u>	Mandatory Pool Participation
<u>Reinsured:</u>	Florida Joint Underwriters Association Pool
<u>Term:</u>	As long as Company writes in state
<u>Premium:</u>	Assumed premium in 2002, \$177,000
<u>Commission:</u>	n/a
<u>Coverage:</u>	Participation based on premium written in state

(2)

<u>Type:</u>	Mandatory Pool Participation
<u>Reinsured:</u>	Mississippi Assigned Risk Plan
<u>Term:</u>	As long as Company writes in state
<u>Premium:</u>	Assumed premium in 2002, \$79,000
<u>Commission:</u>	n/a
<u>Coverage:</u>	Participation based on premium written in state

(3)

<u>Type:</u>	Mandatory Pool Participation
<u>Reinsured:</u>	National Workers Compensation Pool
<u>Term:</u>	As long as Company writes in states covered by the pool
<u>Premium:</u>	Assumed premium in 2002, \$1,550,000
<u>Commission:</u>	n/a
<u>Coverage:</u>	Participation based on premium written in states that are not covered by specific associations or pools.

Ceded:

(1)

Type:

Reinsurer:

Term:

Premium:

Quota Share

FCCI Insurance Company

Effective October 1, 1998 until canceled

The Company shall cede Written Premiums applicable to new and renewal policies during the period this Agreement is in effect in accordance with the schedule below. In addition to the schedule, the Company shall pay 10% of the catastrophe reinsurance premium secured by the Reinsurer.

<u>Line of Insurance</u>	<u>CEDING PERCENTAGES</u>		
	<u>Primary Excess</u>		<u>Total</u>
Workers' Compensation and Employers' Liability	77.533%	13.852%	91.385%
Umbrella Liability	100%	0%	100%
Casualty Business Excluding (1) workers' compensation and employers' liability and (2) umbrella liability	80.73%	10.30%	91.03%
Property Business	76.086%	15.46%	91.546%

Commission:

Provisional commission allowances for reinsurance coverage of the primary layer are as follows:

<u>Line of Insurance</u>	<u>Provisional Commission Allowance</u>
Workers' Compensation and Employers' Liability	32.5%
Umbrella Liability	30%
Casualty Business excluding (1) workers' compensation and employers liability and (2) umbrella liability	32.5%
Property Business	30%

On all primary layer return premiums the Company shall return to the Reinsurer the provisional commission allowance. The provisional commission allowance shall be subject to adjustment at

the end of each calendar year based upon 90% of the actual total expenses incurred by the Company during the applicable calendar year.

Coverage: 90% quota share participation of the Primary Layer of insurance and 100% quota share of the Excess Layer of insurance as follows:

Line of Insurance	<u>Primary Layer</u>		<u>Excess Layer</u>		
	<u>Reinsurance Participation</u>	<u>Maximum Reinsurer Liability</u>	<u>Excess Attachment Point</u>	<u>Excess Limit</u>	<u>Reinsurer Participation</u>
Workers' Compensation & Employers Liability	90%	\$225,000	\$225,000	Unlimited	100%
Umbrella Liability	100%	\$5,000,000	N/A	N/A	N/A
Casualty Business excluding (1) workers' comp & employers liability and (2) umbrella liability	90%	\$900,000	N/A	N/A	N/A
Property Business	90%	\$900,000	\$1,000,000	\$9,000,000	100%

The reinsurance agreement between the Company and FCCI contains a clause that states "it is the intention of the parties for the ceded premium to be remitted on a current basis to the Reinsurer [FCCI] and the paid loss and paid allocated loss adjustment expense recoverables to be remitted on a current basis to the Company." However, the parties may agree to follow one or more of the following procedures to best achieve the "parties' mutual objectives":

1. Settle amounts due the other party within 30 days after receipt of statement;
2. If mutually agreed, the Company will withhold ceded premium payments to FCCI to the extent necessary to reduce net "Schedule F" recoverables.
3. If mutually agreed, FCCI will provide competent security in an amount due the Company for return premiums, paid loss and loss adjustment expense recoverables, loss and loss adjustment expense reserves, and unearned premium reserves.

The NAIC Accounting Practices and Procedures manual states that provisions in the reinsurance agreement which would have the effect of deferring FCCI's obligation to reimburse the Company for covered losses, such as floating retention levels, "last dollar paid" arrangements, or multiple year retentions, generally cause the agreement to fail

the timing risk requirement.

While the eventual recoverability of the amounts due from FCCI does not appear to be in doubt, it appears that the Company and FCCI have significant control over the timing of the payment of both premiums and losses under the reinsurance agreement. Thus, the agreement is deemed to fail the timing risk test, and therefore, may not effectively transfer risk.

The amounts due from the reinsurer under this agreement are collateralized by funds held under a trust agreement dated December 12, 2001, between the Company, FCCI Insurance Company and the Bank of New York.

COMMISSION EQUITY

The ceded Quota Share Reinsurance Agreement in effect at December 31, 2002 is on a gross written premium basis with a provision allowing ceding commission income to be adjusted to a minimum amount equal to 90% of the actual expenses incurred by the Company during the applicable calendar year. The amount included in underwriting expenses for this provision was \$18,652,471 in 2002. The commission equity on unearned premium reserves at December 31, 2002 was \$7,765,162 on ceded business. The Company's treatment of such amounts appears to comply with SSAP No. 62, paragraphs 50 and 51.

RETIREMENT PLAN AND OTHER EMPLOYEE BENEFITS

As of December 31, 2002, the Company had no employees. All services are performed through FCCI Services, Inc. (FSI), an affiliated member of the holding company.

The employees of FSI are eligible to participate in various benefit plans offered. The basic benefit plans provided for health, dental, life, and disability coverage. Vision care, pre-paid legal services, and long-term care coverage are provided as optional benefits.

Employees who meet eligibility requirements and who have been employed for at least six months may participate in a 401(k) Plan managed by The Vanguard Group which offers a selection of investment options. Based on the holding company's financial results each year, a discretionary profit sharing contribution may be made to each account as well.

LOSS EXPERIENCE

The loss experience of the Company for the period under examination, as reported in its annual statements filed with the Department of Commerce and Insurance, is as follows:

<u>Year</u>	<u>Losses</u>		<u>Premiums</u>	
	<u>Incurred</u>	<u>LAE Incurred</u>	<u>Earned</u>	<u>Loss Ratio</u>
2000	1,623,710	(437,356)	\$2,426,151	48.9%
2001	4,473,660	1,009,488	6,452,431	85.0%
2002	5,765,032	1,046,598	5,501,138	123.8%
Total	11,862,402	1,618,730	14,379,720	93.8%

ACCOUNTS AND RECORDS

The primary location of the Company's books and records is 6300 University Parkway, Sarasota, Florida. All accounting functions are performed under the Company's Management Services Agreement. Accounting records and supporting data are compiled in accordance with established insurance accounting practices and generally accepted accounting principles. All of the Company's accounts and records are maintained on an electronic data processing system.

During the course of the examination, accounts were verified and records reviewed using various tests and procedures deemed necessary to establish values for assets and liabilities appearing in the Company's annual statements. Test checks for selected periods were made of premium receipts, investment income, including interest due and accrued, and disbursements, including claim payments, to the extent deemed necessary. Additionally, premium tax returns and federal income tax returns were examined.

Accounting records conform to generally accepted insurance accounting practices and appear to properly reflect the operations during the period under examination and the status of the Company at the date of examination.

An audit of the Company is conducted annually by an independent accounting firm.

The Company's Risk Based Capital Report was reviewed.

STATUTORY DEPOSITS

In compliance with statutory requirements, the Company maintained the following deposits at December 31, 2002.

<u>Where Deposited and Description</u>	<u>Par Value</u>	<u>Statement Value</u>	<u>Market Value</u>
Arkansas, Special Deposit			
UST Notes, 4.63%, Due 5/15/06	\$ 120,000	\$ 123,652	\$ 129,413
Louisiana, Special Deposit			
Bank One CDs, 1.19%	20,000	20,000	20,000
North Carolina, Special Deposit			
US Treas. Money Market Fund	575,000	575,000	575,000
South Carolina, Special Deposit			
UST Notes, 5.63%, Due 2/15/06	150,000	156,524	166,125
Virginia, Special Deposit			
FHLB, 6.24%, Due 11/08/05	325,000	317,497	360,776
US Dept. of Labor, Special Deposit			
UST Notes, 3.63%, Due 3/31/04	400,000	399,638	411,500
UST Notes, 4.75%, Due 2/15/04	400,000	400,868	415,625
Arizona, Special Deposit			
UST Notes, 5.5%, Due 5/31/03	120,000	120,086	122,100
Florida, General Deposit			
UST Notes, 6.5%, Due 10/15/06	225,000	247,928	258,469
Georgia, General Deposit			
UST Notes, 6.5%, Due 10/15/06	115,000	126,719	132,106
Tennessee, General Deposit			
UST Notes, 7.0%, Due 7/15/06	525,000	590,550	608,672
FHLB, 6.24%, Due 11/08/05	<u>975,000</u>	<u>952,491</u>	<u>1,082,327</u>
Totals	<u>\$ 3,950,000</u>	<u>\$ 4,030,953</u>	<u>\$ 4,282,113</u>

These deposits were verified by written confirmations. With the exception of the special deposits held by the States of Virginia and Arizona, and the U.S. Department of Labor, the statutory deposits are admitted assets in accordance with Tenn. Code Ann. §56-1-405. The remaining deposits were reported as non-admitted by the Company in its Annual Statement.

AGREEMENTS WITH PARENT, SUBSIDIARIES AND AFFILIATES

- A) Under a "Federal and State Income Tax Allocation Agreement " effective as of the first day of the tax year ending December 31, 2000, between the Company, its parent and other affiliates , the Company's federal income tax return is consolidated with its parent. This agreement appears to be standard in form and fair to each party. It does not appear that this agreement was submitted for approval as required by Tenn. Code Ann. §56-11-206(a)(2)(D).
- B) The Company has a service agreement with Florida Employers Insurance Service Corporation, now known as FCCI Services, Inc. (FSI), an affiliated company. The agreement was executed February 1, 1990, and has a term of five years and is automatically extended for one year on each succeeding January 1 unless either party gives written notice that it desires to terminate the automatic extension. FSI provides the Company all product support and general and administrative services for a fee. The terms of the agreement appear to be fair to both parties. It does not appear that this agreement was submitted for approval as required by Tenn. Code Ann. §56-11-206(a)(2)(D).

LITIGATION

As of December 31, 2002, the Company had no pending litigation, other than that arising out of the normal course of business, which would adversely affect the financial condition of the Company.

FINANCIAL STATEMENT

There follows a statement of assets, liabilities and statement of income at December 31, 2002, together with a reconciliation of capital and surplus for the period under review, as established by this examination:

ASSETS

	<u>Ledger Assets</u>	<u>Non-Ledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>
Bonds	\$11,603,840		\$1,237,881	\$10,365,959
Cash and short-term investments	9,616,230			9,616,230
Premiums and agents' balances in course of collection	5,596,896		1,348,094	4,248,802
Premiums and agents' balances booked but Deferred and not yet due	10,395,038		61,324	10,333,714
Amounts receivable under high deductible Policies	60,431			60,431
Federal income recoverable	1,085,466		724,398	361,068
Interest, dividends and real estate income due and accrued	137,031			137,031
Receivable from parent, subs and affiliates	368,277		368,277	0
Aggregate write-ins for other than invested assets	<u>1,185,985</u>		<u>437,824</u>	<u>748,161</u>
Totals	<u>\$40,049,194</u>	<u>\$0</u>	<u>\$4,177,798</u>	<u>\$35,871,396</u>

LIABILITIES, SURPLUS, AND OTHER FUNDS

Losses		\$6,691,154
Reinsurance payable on paid loss and loss adjustment expenses		848,085
Loss adjustment expenses		956,243
Commissions payable, contingent commission and similar charges		1,425,444
Taxes, licenses and fees (excluding federal and foreign income taxes)		1,615,219
Federal and foreign income taxes (excluding deferred taxes)		217,541
Unearned premiums		2,042,685
Advance premiums		114,342
Funds held by company under reinsurance treaties		11,058,391
Amounts withheld or retained by company for account of others		441,248
Remittances and items not allocated		10,445
Payable to parent, subsidiaries and affiliates		1,531,400
Aggregate write-ins for liabilities (retroactive reinsurance reserves)		<u>6,878</u>
Total Liabilities		<u>26,959,075</u>
Common capital stock	\$2,500,000	
Gross paid in and contributed surplus	9,290,293	
Unassigned funds (surplus)	<u>(2,877,972)</u>	
Total capital and surplus		<u>8,912,321</u>
Totals		<u>\$35,871,396</u>

STATEMENT OF INCOME

Underwriting Income

Premiums earned	<u>\$5,501,136</u>
Deductions:	
Losses incurred	5,765,032
Loss expenses incurred	1,046,598
Other underwriting expenses incurred	<u>1,834,902</u>
Total underwriting deductions	<u>8,646,532</u>
Net underwriting gain or (loss)	<u>(3,145,394)</u>

Investment Income

Net investment income earned	1,281,712
Net realized capital gains or (losses)	<u>(204)</u>
Net investment gain or (loss)	<u>1,281,508</u>

Other Income

Net gain (loss) from balances charged off	(125,118)
Finance and service charges not included in premiums	102,807
Aggregate write-ins for miscellaneous income	<u>636</u>
Total other income	<u>(21,675)</u>
Net income before federal income taxes	(1,888,561)
Federal and foreign income taxes incurred	<u>217,541</u>
Net Income	<u>\$(2,103,102)</u>

RECONCILIATION OF CAPITAL AND SURPLUS
FOR THE PERIOD UNDER EXAMINATION

Surplus as regards policyholders December 31	<u>2000</u>	<u>2001</u>	<u>2002</u>
Previous Year	<u>\$10,528,357</u>	<u>\$11,630,545</u>	<u>\$11,289,677</u>
Net Income	1,473,544	49,245	(2,103,102)
Change in net deferred income tax		398,261	534,960
Change in Nonadmitted assets	(256,356)	(1,055,621)	(809,214)
Cumulative effect of changes in accounting principles		267,247	
Aggregate write-ins for gains and losses in surplus	(115,000)		
Change in surplus as regards policyholders for the year	<u>1,102,188</u>	<u>(340,868)</u>	<u>(2,377,356)</u>
Surplus as regards to policyholders December 31			
Current Year	<u>\$11,630,545</u>	<u>\$11,289,677</u>	<u>\$ 8,912,321</u>

ANALYSIS OF CHANGES IN FINANCIAL STATEMENT AND COMMENTS
RESULTING FROM EXAMINATION

<u>Item</u>	<u>Amount</u>
Bonds	\$10,365,959

The above amount reflects an increase of \$160,298 from the amount stated in the annual statement.

This amount consists of special deposits which are held by various states in which the Company does business. The Company has reported such deposits as non-admitted. However, Tenn. Code Ann. § 56-1-405 states, in part, that "The commissioner...may credit any deposits of funds of the company set apart as security for a particular liability, or any deposits of funds of the company that are deposited for the purpose of meeting the requirements for doing business in another state or commonwealth." Therefore, the amounts which are deposited with the various states are admitted to the extent that the Company has direct written premium as an offsetting liability.

Cash and short-term investments	\$9,616,230
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The above amount reflects an increase of \$595,000 from the amount stated in the annual statement. This amount consists of special deposits which are deemed to be admitted assets as described above.

Receivable from parent, subsidiaries and affiliates	\$0
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The above amount reflects a reduction of \$368,277 from the amount stated in the annual statement.

This amount is premium which is collected via a lockbox arrangement with the Company's parent and affiliates. Settlement of the amount in the lockbox to the Company has been taking place quarterly. The "Order Adopting Examination Report as Filed" issued by the Commissioner of the Department of Insurance on January 26, 2001, directed the Company to comply with Tenn. Code Ann. § 56-11-206 respecting transactions with a holding company system by formalizing in writing the lockbox arrangement with its indirect parent, FCCI Insurance Company. This written agreement requires monthly settlement of balances. The outstanding balance was not settled within ninety days and is required to be reported as non-admitted by the NAIC Annual Statement instructions. Therefore, the total \$368,277 is nonadmitted.

Other expenses**(\$-0-)**

The above amount reflects a reduction of \$1,525,769 from the amount stated in the annual statement. This amount is a reclassification to "Payable to parent, subsidiaries and affiliates".

The \$1,525,769 owed to FCCI Services, Inc.(FSI) under an intercompany service agreement for the providing of servicing claims, managing payroll and providing clerical and administrative assistance was reclassified to the liability account "Payable to parent, subsidiaries and affiliates". This more accurately reflects SSAP No. 67 which states "A liability shall be recognized and identified as due to affiliates for expenditures incurred on behalf of the reporting entity by a parent, affiliates or subsidiaries".

Payable to parent subsidiaries and affiliates**(\$1,531,401)**

The above amount reflects an increase of \$1,525,769 from the amount stated in the annual statement.

This amount is a reclassification from "Other expenses" of the amount owed to FCCI Services, Inc. (FSI) under an intercompany service agreement for servicing claims, managing payroll and providing clerical and administrative assistance. This more accurately reflects SSAP No. 67 which states "A liability shall be recognized and identified as due to affiliates for expenditures incurred on behalf of the reporting entity by a parent, affiliates or subsidiaries".

Unassigned funds (surplus)**(\$2,877,972)**

The amount of this item is \$387,021 more than the amount reflected in the Company's annual statement. The increase is the net result of the changes in the above items.

**SUMMARY SCHEDULE FOR "ANALYSIS OF CHANGES
IN FINANCIAL STATEMENT AND COMMENTS RESULTING FROM
EXAMINATION" AS THEY AFFECT SURPLUS**

The following depicts the change in surplus as outlined in the previous section of this report:

<u>Item</u>	<u>Surplus</u>	
	<u>Increase</u>	<u>Decrease</u>
Bonds	\$ 160,298	
Cash and short-term investments	595,000	
Receivable from parent, subsidiaries and affiliates		\$ 368,277
Other expenses	1,525,769	
Payable to parent, subsidiaries and affiliates		1,525,769
Totals	\$2,281,067	\$1,894,046
Net change in surplus	<u>\$ 387,021</u>	

COMMENTS AND RECOMMENDATIONS

Comments:

- The Company is a party to an intercompany service agreement for the providing of servicing claims, managing payroll and providing clerical and administrative assistance with FCCI Services, Inc. (FSI) an affiliate corporation. To more accurately reflect NAIC Accounting Practices, the Company should record any amount owed to FSI on the liability line captioned, "Payable to parent, subsidiaries and affiliates". This more accurately reflects SSAP No. 67 which states "A liability shall be recognized and identified as due to affiliates for expenditures incurred on behalf of the reporting entity by a parent, affiliates or subsidiaries".

The intercompany service agreement calls for settlement on a monthly basis. Settlement has been occurring quarterly. The Company should either settle monthly or amend the agreement to indicate settlement on a quarterly basis.

- In July of 1999, the Company entered into a lockbox arrangement with its parent, FCCI Insurance Company whereby premium remittances are deposited into a fiduciary account under the name of FCCI Insurance Company. The funds are electronically identified, using encoded remittance advises. The Company and FCCI have formalized the lockbox arrangement with a written agreement that specifies that amounts due should be settled on a monthly basis. Transfer has been taking place on a quarterly rather than a monthly basis. The Company should comply with the agreement's terms.

Recommendations:

- The Quota Share Reinsurance Agreement between the Company and its parent, FCCI Insurance Company was modified by virtue of an endorsement effective January 1, 2002 and was not submitted for department approval as required under TCA 56-11-206(a)(2)(C). The Company should submit all agreements for approval prior to their use.
- The Federal and State Income Tax Allocation Agreement between the Company, its parent, and affiliates was not submitted for department approval as required under TCA 56-11-206(a)(2)(D). The Company should submit all agreements for approval prior to their use.
- The service agreement with Florida Employers Insurance Service Corporation, now known as FCCI Services, Inc. (FSI), an affiliated company was not submitted for department approval as required under TCA 56-11-206(a)(2)(D). The Company should submit all agreements for approval prior to their use.

CONCLUSION

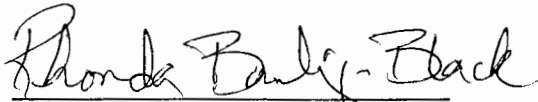
Insurance examination practices and procedures, as promulgated by the National Association of Insurance Commissioners, have been followed in connection with the verification and valuation of assets and the determination of liabilities of National Trust Insurance Company, a Tennessee Corporation with administrative offices in Sarasota, Florida.

In such manner, it was determined that, as of December 31, 2002, the Company had admitted assets of \$35,871,396 and liabilities, exclusive of capital, of \$26,959,075. Thus, there existed for the additional protection of the policyholders, the amount of \$8,912,321 in the form of paid-up capital, gross paid-in and contributed surplus and unassigned funds (surplus).

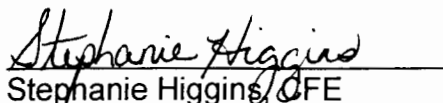
The courteous cooperation of the officers and employees of the Company extended during the course of the examination is hereby acknowledged.

In addition to the undersigned, Juli-Kay Baumann, ARM, ARe, AIE, CFE, CPCU, participated in the completion of this examination.

Respectfully submitted,



Rhonda Bowling-Black, CFE
Examiner-in-Charge
State of Tennessee
Southeastern Zone, NAIC



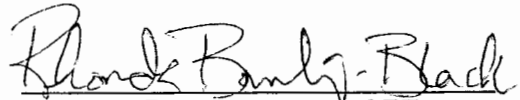
Stephanie Higgins, CFE
Insurance Examiner
State of Tennessee
Southeastern Zone, NAIC



Amy J. Maggard
Insurance Examiner
State of Tennessee
Southeastern Zone, NAIC

AFFIDAVIT

The undersigned deposes and says that he has duly executed the attached examination report of National Trust Insurance Company dated August 17, 2004, and made as of December 31, 2002, on behalf of the Tennessee Department of Commerce and Insurance. Deponent further says she is familiar with such instrument and the contents thereof, and that the facts therein set forth are true to the best of his knowledge, information and belief.



Rhonda Bowling-Black, CFE
Insurance Examiner
State of Tennessee
Southeastern Zone, NAIC

Subscribed and sworn to before me

this 17th day of

August, 2004

Notary

Glen M. Dorsey

County

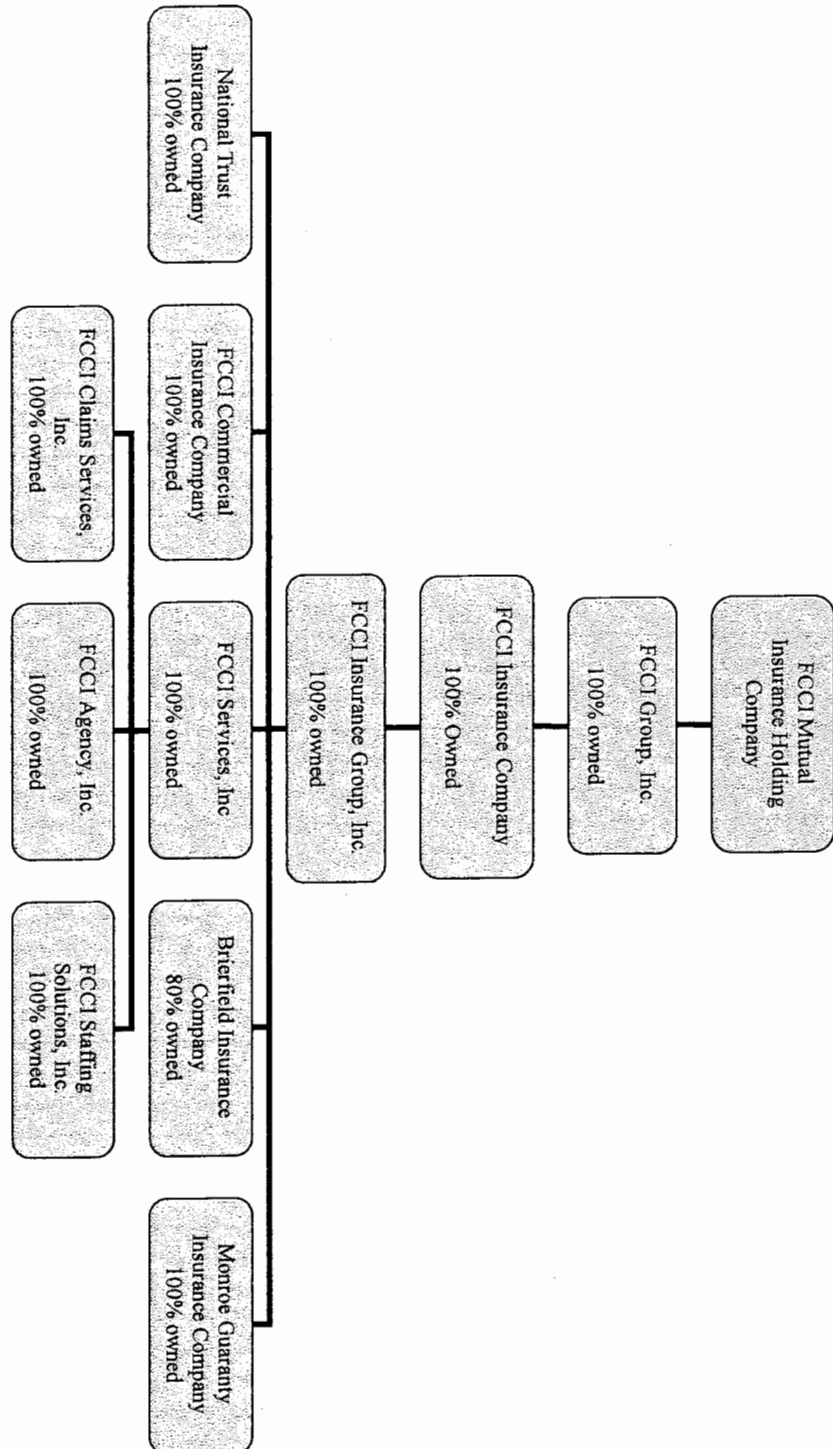
Davidson

State

Tennessee

Commission Expires 03/25/06

ORGANIZATIONAL CHART



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SEP 22 2004

Dept. Of Commerce & Insurance
Company Examinations

September 2, 2004

Mr. Don Spann, CFE
Insurance Examination Director
State of Tennessee
Department of Commerce and Insurance
500 James Robertson Parkway
Nashville, TN 37243

**RE: Financial Condition Examination of National Trust Insurance Company
("NTI" or the "Company") as of December 31, 2002**

Dear Mr. Spann:

We have received and reviewed the above referenced examination report. Following is our response to certain items in the report.

1. Comment Pg. 27- Service Contract Inter-Company Balances- Classification on Balance Sheet

Effective with the June 30, 2004 quarterly statement, the Company began classifying the balance due to FSI on the liability line captioned "Payable to parent, subsidiaries and affiliates." However, note that this presentation will distort cash flow for Other underwriting expenses as the expense accruals associated with the service agreement are charged to Other underwriting expenses while the related liability (and changes therein) will be classified as an inter-company balance instead of Other expense liability. Please see annual statement, Page 11 - Part 3 - Expenses, Col. 2, Lines 25 - 30. Specifically, Lines 26 and 27 - Unpaid expenses, do not include "Payable to parent, subsidiaries and affiliates."

2. Comment Pg. 27 - Service Contract - Settlement Frequency

Your comment is noted. The Company began settling these balances monthly on 9/1/04. We will continue to do so going forward.

3. Comment Pg. 27 - Lockbox Arrangement - Settlement Frequency

In some cases the Company did not receive a monthly physical settlement of amounts due from FCCI Insurance Company ("FCCI") under the lockbox agreement. However, at all times during the period under examination, the Company had an offsetting balance of at

least \$11 million (compared to an average lockbox receivable of \$2 million) owed to FCCI in the form of ceded balances payable under the 90/10 quota-share agreement. So while cash was not exchanged each month, the balances were effectively settled through offsetting balances. Accordingly, we respectfully request that this comment be removed from the report.

4. Recommendation Pg. 27 - Quota-Share Reinsurance Agreement – Submission for Approval

Find enclosed the main contract and all endorsements for your review and approval.

5. Recommendation Pg. 27 - Federal and State Income Tax Allocation Agreement – Submission for Approval

Find enclosed the contract for your review and approval.

6. Recommendation Pg. 27 - Service Agreement with FCCI Services, Inc.

The service agreement with FSI was replaced with a new contract in 2003. The Company filed for approval on September 30, 2003 and received approval of the new contract on November 1, 2003.

7. Risk Transfer Pgs. 15-16 – 90/10 Quota-Share Agreement

The report states in the Reinsurance section beginning at the bottom of Page 15 the following:

The NAIC Practices and Procedures manual states that provisions in the reinsurance agreement which would have the effect of deferring FCCI's obligation to reimburse the Company for covered losses, such as floating retention levels, "last dollar paid" arrangements, or multiple year retentions, generally cause the agreement to fail the timing risk requirement.

While the eventual recoverability of the amounts from FCCI does not appear to be in doubt, it appears that the Company and FCCI have significant control over the timing of the payment of both premiums and losses under the reinsurance agreement. Thus the agreement is deemed to fail the timing risk test, and therefore may not effectively transfer risk.

We disagree that the Company's reinsurance agreement with FCCI fails risk transfer. The contract contains none of the timing risk factors mentioned above and the mere appearance of significant control over the timing of payment of premiums and losses does not constitute failure of timing risk. In addition, at the request of the Department, FCCI created a \$100 million trust fund in December 2001 to secure the Company's reinsurance balances, including ceded reserves. Finally, this reinsurance contract has been in effect since 1998, and no statutory audit or Tennessee examination has ever identified risk transfer as a concern.

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Dept. of Commerce & Insurance
Financial Affairs/Analytical

For these reasons we respectfully request that the risk transfer language be removed or modified to more accurately reflect that the 90/10 quota-share contract does effectively transfer risk.

Should you have any questions please call me at 941-907-7643 or email me at cshoucair@fcci-group.com.

Sincerely,

A handwritten signature in black ink, appearing to read 'Chris', with a long horizontal flourish extending to the right.

Chris Shoucair
Director, Financial Reporting

Enclosures

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**Dept. of Commerce & Insurance
Financial Affairs/Analytical**